

Portability of Benefits, Job Changes, and the Role of Government Policies

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Foreword

The Task Force on Reconstructing America's Labor Market Institutions

The world of work is changing, but the traditional structures governing the labor market, in place since the New Deal, no longer serve the needs of workers and their families or of corporations seeking to compete in a global economy.

The mandate of the Task Force on Reconstructing America's Labor Market Institutions is to provide a body of evidence that helps policymakers and practitioners structure a national discussion on how to update the nation's labor market institutions—resolving the mismatch between a fundamentally new economy and a set of inappropriate intermediaries, laws, and corporate practices.

The efforts of Task Force members are divided among three working groups, each charged with examining a particular aspect of this labor market mismatch: the Working Group on the Social Contract and the American Corporation, the Working Group on Low-Income Labor Markets, and the Working Group on America's Next Generation Labor Market Institutions.

"Symposium on Changing Employment Relations and New Institutions of Representation," Task Force and U.S. Department of Labor Conference, May 25-26, 1999

As part of the U.S. Secretary of Labor's project, "The Workforce/Workplace of the Future," the U.S. Department of Labor joined with the Task Force to sponsor a symposium on changing employment relations and new institutions of representation emerging in the new economy. The meeting was organized around several key questions:

- What new strategies and structures are being developed to better represent today's workforce?
- How is the new social contract developing in selected "best practice" firms?
- How are industrial unions and corporations redefining their roles to meet the challenges of today's economy and workforce?

In addressing these questions, symposium participants discussed: the limits of enterprise-based social contracts; labor market institutions that are developing beyond the enterprise—including community-level strategies and alternative models such as professional organizations and social identity groups; and new union strategies for building capacity and rethinking structures.

This paper, written for the symposium by Robert Clark of North Carolina State University, informed the discussion of representation beyond the enterprise—specifically, labor market strategies for a mobile workforce in the form of portable pensions.

Abstract

Among the most important and valuable employee benefits are retirement plans and health insurance. Yet, changes in the industrial structure of the economy and the composition of the labor force raise questions about the future of long-term careers with a single company and about the need for the portability of benefits for employees. If the American workforce in the twenty-first century becomes characterized by less loyalty between workers and firms, more jobs in one person's working career, and greater turnover, such trends will have a significant impact on how employers define compensation and the provision of benefits.

Written for the May 25-26, 1999, "Symposium on Changing Employment Relations and New Forms of Worker Representation"—co-sponsored by the Task Force on Reconstructing America's Labor Market Institutions at MIT and the U.S. Department of Labor—this paper examines the portability of pension benefits and health insurance coverage, recent trends in these benefits, and the significant role of government regulations in the provision of portable employee benefits. It addresses questions such as: How will employee benefits evolve in a world of reduced job tenure and increased turnover? How are current trends in the characteristics and provision of pension plans and health insurance altering the portability of such benefits? How do current government policies affect the structure of pensions and health insurance and their portability? Finally, the paper ends with a discussion of the new benefit regulations and policies needed to provide for more portable benefits.

Introduction

In addition to cash wages and salary, employers provide a variety of benefits to their employees in exchange for their labor services. Among the most important and valuable employee benefits are retirement plans and health insurance.¹ Workers who are fired, laid off, or who quit voluntarily often suffer substantial losses in the expected value of their pension benefits, may lose health insurance coverage, and may lose the promise of health insurance in retirement. As a result, job changers suffer capital losses in the lifetime value of these benefits. The prospect of such losses in lifetime welfare tends to reduce the likelihood that employees will change jobs and may alter the timing of retirement.

If the lack of portability of employee benefits impedes productivity improving job changes, individual and aggregate welfare may be reduced. Policy makers are concerned about the possibility of benefit-induced job lock and the role of government policies in the promoting the use of benefits that impose such costs on mobile workers. This paper examines the portability of pension benefits and health insurance coverage, recent trends in these benefits, and the significant role of government regulations in the provision of employee benefits.

The U.S. labor market is rapidly changing. Employment in the service sector is expanding while manufacturing is declining in relative importance. For example, employment in the service-producing sectors of the economy increased from 74.2 million workers in 1986 to 94.3 million in 1996 while employment in the goods-producing sectors actually fell slightly from 24.5 to 24.4 million workers. As a result, employment in the service sectors increased from 66.6 percent of total U.S. employment in 1986 to 71.2 percent in 1996 (Franklin, 1997).² The significance of firm specific skills often associated with long career jobs may be diminishing in response to this change in the employment mix.

The composition of the labor force is also changing as women and minorities represent a larger share of all workers. In 1996, women accounted for 46.2 percent of the labor force compared to 40.5 percent in 1976. Nonwhites composed 15.6 percent of the labor force in 1996, an increase from only 11.8 percent in 1976 (Fullerton, 1997). These demographic groups have traditionally been associated with higher job turnover and lower tenure. As a result of these changes in the industrial structure of the economy and the composition of the labor force, the future of long careers with a single company is now being questioned. The American labor force

in the twenty-first century may be characterized by less loyalty between workers and firms, more jobs per working career, and greater turnover.³

Key questions concerning changes in the employment contract and the evolving characteristics of pension plans and health insurance include:

- How will employee benefits evolve in a world of reduced job tenure and increased turnover?
- How are current trends in the characteristics and provisions of pension plans and health insurance altering the portability of these benefits?
- What new strategies will firms develop to hire, retain, and replace a quality workforce?
- How do current government policies affect the structure of pensions and health insurance and the portability of these benefits?
- What new benefit regulations and policies are needed in the twenty-first century to provide for more portable employee benefits?

These important questions are examined in this paper as we seek to determine how organizations are redefining compensation to meet the challenges of the changing American labor force. The analysis will focus on the portability of pension and health plans and the need for new policies concerning the provision of more portable benefits.

Compensation, HR Policies, and Job Tenure

Employee benefits are an important component of total compensation. Some benefits provide significant noncash current compensation while others promise deferred income streams after the worker leaves the firm. Individuals assess the value of these benefits when considering initial job offers, when deciding whether to quit the firm, and when deciding on their retirement age. The conditional nature of some employee benefits and their lack of portability across employers can result in considerable differences in lifetime income and welfare depending on whether workers remain with a single company throughout their work life or whether their career is marked by repeated job changes.

It is important to understand the role of employee benefits and how the lack of portability affects the welfare of workers. This requires an understanding of existing company policies and the effect of government regulations on employee benefits. This section begins our analysis by examining the portability of today's retirement plans and health insurance and how government policies alter the structure of these benefits.

If workers were paid entirely with cash in a spot labor market, each worker and each firm could assess the best job match for them each period. Movement across firms would not involve the loss of any promised compensation and portability would not be an issue. While such compensation structures may have characterized earlier U.S. labor markets, the second half of the twentieth century has seen the development of more complex systems of compensation including the use of pension plans, health insurance, and other types of employee benefits as important components of total compensation. The introduction of employee benefits has been due to a variety of factors including the lack of national programs for pensions and health insurance, government tax policy, the desire by employers to tie workers to firms in an effort to reduce labor costs associated with turnover, union interests in negotiating a wider range of compensation, and the ability of workers to benefit from group rates on health insurance.

Government regulations associated with the provision of pension plans and health insurance generally is linked to the preferential tax status they receive. In the case of pensions, company and worker contributions to pension plans are not taxed as current income for the purposes of federal and state income taxes provided the plan meets certain federal standards. Instead, retirement income is taxed when it is received often many years after it is earned.⁴ In

addition, pension contributions are not subject to payroll taxes. The avoidance of payroll taxes and the deferment of income taxes means that workers covered by pension plans can receive greater total compensation per dollar of employer costs when a portion of compensation is provided in the form of pension contributions.

Company expenditures for health insurance also are not subject to either income or payroll taxes. Payments for health insurance permanently avoid both types of taxes. In exchange for qualifying for this preferential tax status, pension and health insurance plans must meet certain standards. These standards require that benefits be offered to a broad range of employees and not just highly compensated employees and managers (nondiscrimination) and in the case of pensions, there are additional vesting, management, and funding requirements that firms must meet (McGill, et. al, 1996).

Portability of Pensions

Pension plans are of two basic types: defined benefit and defined contribution.⁵ In a defined benefit plan, workers are promised a specific benefit in retirement. The benefit is typically based on years of service times a percent of average salary during the final working years.⁶ Defined contribution plans provide for periodic contributions into an individual pension account for each worker. The contributions may be made by the firm and/or the worker. The eventual retirement benefit is dependent on the amount of the contributions and the rate of return on the individual's retirement assets.⁷

Defined benefit plans are considerably less portable than defined contribution plans and therefore, job changes may result in substantial reductions in retirement benefits. Current regulations require that promised benefits must be vested after five years of service.⁸ This means that workers leaving the firm with fewer than five years of service will receive zero retirement benefits. Workers with more than five years of service will receive promised benefits in accordance with the existing benefit formula and retirement age requirements. For most workers, this means that benefits are determined on the basis of average earnings before leaving the firm. Thus, when a worker leaves the firm at a relatively young age, the future pension benefit is frozen in nominal terms until benefits are actually received in retirement.⁹ Over time, as consumer prices increase and the earnings rise, the real and relative value of this benefit declines. It is easily shown that workers with the same lifetime earnings who move across firms

with identical retirement plans will accumulate lower total pension benefits than workers who remain with the same firm throughout their careers (Clark and McDermid, 1988).

Defined benefit pension plans offer workers retirement income conditional on their meeting certain age and service requirements. As a results, these pension plans also can be used to alter worker behavior such as effort on the job (Lazear, 1979), the timing of retirement (Quinn, Burkhauser, and Myers, 1990), and the probability of quitting (Allen, Clark, and McDermid, 1993). Workers desire employer-provided pensions primarily because of the tax advantages associated with this type of retirement savings and the ease of saving prior to receiving the money in their paychecks.

In contrast, workers covered by defined contribution plans typically do not incur such capital losses when they change employers. In general, these workers have a legal claim on a pension account in which all pension contributions have been invested. If the funds remain in the account after the worker leaves the firm, the account will continue to grow with the returns on the invested assets. Alternatively, the funds can usually be withdrawn from the pension of a former employer and rolled over into an IRA or a new pension account.¹⁰ In either case, the worker who has changed jobs retains the full value of the pension funds. Thus, in general, defined contribution plans are completely portable and workers can change jobs without the loss of pension benefits.

This analysis shows that issues relating to the portability of retirement benefits are primarily limited to defined benefit plans. Thus, two primary areas of concern remain. First, how portable are current defined benefit pension benefits and what policies should be considered to make these benefits more portable? Second, what is the mix of pension coverage among current workers and what policies should be considered to alter this mix? Of course, workers covered by generous defined contribution plans who are considering a job change must assess the likelihood that their new employer will offer a pension plan. This assessment of the full compensation may affect mobility decisions.

Portability of Health Insurance

The United States does not have a national system of health care providing insurance coverage to all of its citizens. Instead, two government programs, Medicare and Medicaid, provide health insurance to the aged and those poorest members of our society. Most Americans

under the age of 65 acquire their health insurance as part of their compensation from their employer. Employer-provided health insurance may be wholly or partly paid by the firm. Workers may have to pay a portion of the health insurance premium, deductibles, and co-payments. The primary advantages of this type of benefit to employees are the access to the group insurance plans, payment with pre-tax dollars, and often the avoidance of qualifying medical exams. Companies provide several different forms of health insurance including fee-for-service plans, preferred provider plans, and health maintenance organizations. Often workers are given the option of choosing which of these plans they would prefer; however, the cost of participation in the various plans may differ.

Company-provided health insurance is not portable. Workers can not retain their coverage under their former company's policy when they change jobs. An exception to this statement is that the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) which allows workers to pay the full cost (102 percent of average cost of their former employers health insurance) and remain covered in their old health plan for up to 18 months. Thus, individuals considering moving to a new employer must consider how long they will be between jobs and whether their prospective new employer offers health insurance. This potential period of not having employer health insurance imposes significant costs on workers who are involuntarily terminated and may deter other workers from leaving their positions. The importance of gaps in health insurance coverage depends on the worker's age, gender, family status, and current health status.

Another problem that often confronted workers attempting to change employers was associated with pre-existing medical conditions and the ability to purchase health insurance after leaving a plan provided by the former employer. The Health Insurance Portability and Accountability Act of 1996 (HIPAA) prevents health plans from applying pre-existing condition limits on newly employed workers.

Workers currently considering leaving an employer that provides health insurance must consider their future employment prospects and whether they will find new employment with another company that offers health insurance or whether they will have to consider purchasing health insurance in the private market. The value of current company-provided health insurance will vary across individuals and the key issue for worker-initiated job changes is the value of the insurance to the worker, not the cost to the employer. Thus, workers thinking about changing

jobs must consider the expected duration of time between jobs, the probability of finding new employment with health insurance, and the importance of any pre-existing health conditions. The enactment of COBRA and HIPPA reduced the importance of these factors but do not eliminate portability concerns associated with health insurance.

Many large companies extend health insurance coverage to their retirees. Individuals who meet qualifying conditions can retire and remain covered by the company health insurance plan. This coverage is especially important to early retirees (those less than 65) who may wish to completely withdraw from the labor force or shift to part-time employment. Some companies terminate retiree health insurance when the retiree reaches age 65 and qualifies for Medicare. Qualifying conditions that specify a certain number of years of service may mean that workers who leave the company after only a few years of service will forfeit future health insurance. This lack of portability would impose costs on mobile workers and may reduce turnover. Active workers covered by employer-provided health plans that do not extend coverage to retirees are more likely to defer retirement until age 65 and the attainment of eligibility for Medicare while workers covered by plans that do extend coverage to retirees are more likely to retire from their career employer prior to age 65 (Madrian, 1994a). These workers may then shift to other full-time jobs, change to part-time employment, or withdraw from the labor force.

Retirement Plans

Pension Coverage

The proportion of the labor force covered by some type of employer-provided pension rose rapidly from 1950 until 1975 when about half of the labor force was included in an employer pension. Since 1975, the percent of the labor force covered by a pension has remained relatively stable with coverage falling slightly in the early 1980s then increasing slightly.¹¹ Examination of Current Population Surveys indicates that in 1993, 57 percent of all civilian workers were employed by companies that sponsored a pension plan and 44 percent of all civilian workers were participating in their company plan (EBRI, 1994).¹² Both of these rates were slightly higher than the participation rates found in the 1980s but were very close to the rates in 1979.

Surveys of individuals and employers yield some general observations concerning participation in company-provided retirement plans. Men are slightly more likely to participate in a pension than women; however, the proportion of women participating in a pension has been increasing while the participation rate of men has been decreasing. Public employees are much more likely to be working for an employer that offers a pension than are private employees and public employees were also more likely to participate in the pension when one was offered. Participation is also higher among private sector workers who meet employment conditions specified by the Employee Retirement Income Security Act of 1974 which include the worker being at least 21 years of age with one or more years of tenure on their current job and working 1,000 or more hours per year.

Participation rates in employer-provided pension plans increase with job tenure, age, and annual earnings. These relationships suggest that as workers age and acquire more tenure, attain better jobs, and have higher earnings, the likelihood that they will be included in an employer pension plan increased. Union members are much more likely to participate in a pension plan than nonunion workers. Big companies are much more likely to offer pension plans than small companies and part-time workers are less likely to be participating in company retirement plans than are full-time workers.

Examining the Employee Benefit Surveys of medium and large firms, small firms (fewer than 100 workers), and state and local governments (see Table 1) illustrates the relatively

stability in overall pension coverage during the 1990s. Approximately 80 percent of full-time employees of firms with more than 100 workers were covered by a pension throughout the 1990s compared to only about 45 percent of employees in smaller firms and 95 percent of state and local government workers. There was no clear trend during the 1990s in the pension coverage rates for any of these workers.

Table 1
Percentage of Full-time Employees Participating in Retirement Plans

Year	Any Pension	Defined Benefit	Defined Contribution
Medium and Large Private Establishments			
1988	80	63	45
1989	81	63	48
1991	78	59	48
1993	78	56	49
1995	80	52	55
1997	79	50	57
Small Private Establishments			
1990	42	20	31
1992	45	22	33
1994	42	15	34
1996	46	15	38
State and Local Governments			
1990	96	90	9
1992	93	87	9
1994	96	91	9

Source: Various years of U.S. Bureau of Labor Statistics, *Employee Benefits in Medium and Large Private Establishments*, *Employee Benefits in Small Private Industry Establishments*, and *Employee Benefits in State and Local Governments*.

Defined Benefit and Defined Contribution Pension Plans

Historically, defined benefit plans were the primary type of retirement plan offered by employers. In the past two decades, there has been a dramatic shift toward greater utilization of defined contribution plans and less reliance on defined benefit plans (see Table 2). Defined contribution plans increased as a proportion of all pension plans from 67 percent in 1975 to 92

percent in 1997. The proportion of active pension participants with primary coverage in a defined contribution plan increased from only 13 percent in 1975 to 42 percent in 1997 (Olsen and VanDerhei, 1997). Further examination of the BLS employee benefit surveys supports these trends. The proportion of full-time workers among employees in medium and large firms covered by a defined benefit plan declined from 63 percent in 1989 to 50 percent in 1997. The decline in coverage by defined benefit plans for employees in small firms was from 20 percent in 1990 to 15 percent in 1996 while coverage among state and local government employees remained stable at approximately 90 percent (see Table 1). In contrast, coverage by defined contribution plans increased from 48 to 57 percent in medium and large plans and from 31 to 38 percent for employees of small firms. These data clearly reveal the dramatic decline in the use of defined benefit plans and the corresponding increase in the coverage by defined contribution plans.

Table 2
Private Pension Plans and Participants

Comparison	1975	1980	1985	1990	1993	1997
Defined contribution plans as percent of all pension plans	67	70	73	84	88	92
Participants in defined contribution plans as percent of all pension participants	26	34	47	50	52	53
Active participants in primary defined contribution plans as percent of all active participants	13	16	30	38	42	42

Source: Olsen and VanDerhei (1997).

The decline in utilization of defined benefit plans has resulted from increased government regulation that has raised the administrative cost of offering defined benefit plans in comparison to defined contribution plans and the introduction of new types of defined contribution plans such as the 401(k) plans (Clark and McDermid, 1990). The increase in relative cost of providing defined benefit plans has fallen most heavily on small firms (Hustead, 1998) and as a result, the decline in the use of defined benefit plans has been greatest among these firms.

Structural changes in the economy such as increased employment in the service sector and in smaller firms along with changes in the composition of the labor force to include more mobile workers have also increased the demand for greater use of defined contribution plans (Gustman and Steinmeier, 1992; Ippolito, 1997). Papke (1999) reports evidence of the direct substitution of defined contribution plans for defined benefit plans as firms terminate defined benefit plans and establish defined contribution plans. The replacement of defined benefit plans that lack portability with defined contribution plans that are completely portable is an important trend as the U.S. economy moves towards a more mobile labor force in the twenty-first century.

401(k) Retirement Plans

The most rapidly growing type of pension plan is the 401(k) plan. These plans allow workers to make pre-tax contributions to a retirement savings account. Worker contributions are voluntary and most plan sponsors provide some type of employer matching contribution. In 1983, only 7 percent of private wage and salary workers were offered a 401(k) plan but this proportion increased to 25 percent in 1988 and further to 35 percent in 1993 (U.S. Department of Labor, 1994a). In 1993, approximately two thirds of all persons offered such a plan chose to participate. Offer and participation rates are much greater for full-time workers. These rates increase with age up to the mid-40s and increase with annual earnings.

In most 401(k) plans, workers must decide whether to make voluntary contributions to the plan and how much to contribute. If the worker makes a contribution, many companies then provide some employer matching of the employee contribution. Having contributed to the 401(k) plan, the employee then must decide how to invest the funds. Typically, plan sponsors provide a variety of investment options including fixed income securities and equities. Income in retirement will depend on when the employee begins to contribute, how much the employee contributes, and the performance of the investments chosen. Research studies show that participation and contribution rates increase with age, job tenure, and earnings. Contributions also depend on plan provisions such as the company match rate (Papke, 1995), education and communication concerning the plan (Clark and Schieber, 1998), and access to the funds prior to retirement through loan provisions (U.S. General Accounting Office, 1997a).

A recent analysis of eighty seven 401(k) plans in 1995 yielded several important observations concerning worker choices in these retirement plans (Clark, Goodfellow, Schieber,

and Warwick, 1998). The proportion of eligible workers who contributed to these plans during 1995 increased with age rising from about two thirds of workers in their 20s to over 80 percent of employees over age 40. Participation rates also increased with annual earnings rising from about 70 percent of workers earning less than \$25,000 to over 90 percent of eligible employees with annual earnings in excess of \$60,000. Employee contributions averaged approximately 7 percent of annual earnings.

Adjusting for age and annual earnings, women were more likely to have made a contribution to the 401(k) plan and in general, contributed a higher percent of their salary to the pension plan. The proportion of pension funds invested in equities decreased with age and increased with annual earnings. Women were not more conservative investors with their retirement monies in plans that did not have company stock as an investment option. In plans with an option for investment in company stock, men tended to invest a larger proportion of their retirement funds in their own employer's stock.

Implications of Changes in Pension Coverage

Only about half the labor force is currently covered by any type of employer pension and this proportion has remained at this level for the past 20 years. While this underestimates the proportion of all workers who will ultimately receive a pension in retirement, the current coverage rate and the stability of this rate over the past two decades indicate that many workers will not receive a company pension in retirement. The stability of the coverage rate suggests that this will not change in the near future.

Coverage data clearly show that persons not accumulating pension credits are low wage workers and persons who work fewer hours per year and fewer years of job tenure during their lifetime. If women continue to have shorter, more irregular working careers, they will continue to accumulate less in defined contribution pension plans than comparable male workers.

The trend toward increased availability of defined contribution plans has several potential implications for future retirement income. Workers who change jobs frequently accumulate lower retirement benefits when they move among firms with defined benefit plans. In contrast, job changes have relatively little impact on eventual retirement benefits of those in defined contribution plans. This implies that in the future, mobile workers may enter retirement with

larger total pension benefits than in the past. The greater portability of the defined contribution plans, especially 401(k) plans, should make job changes easier and less costly in the future.

However, defined contribution plans place greater responsibility and investment risk on the individual worker. Most employees of firms providing defined benefit plans are automatically covered by the plan and they do not have to choose to reduce current income in order to save for retirement. In contrast, participants in many defined contribution plans and especially 401(k) plans must decide how much to contribute to the plan each pay period. Low wage workers are less likely to be employed by firms that offer 401(k) plans and when offered, they are less likely to choose to participate in the plan. If they wait until middle age to participate or if they contribute too little, they will have relatively low retirement benefits.

Participants in defined contribution plans must also decide how to invest their retirement funds. Selecting investments with low rates of returns will also lead to lower retirement benefits. Participants in these plans also may have access to the retirement funds prior to their retirement through loans or lump sum distributions at the time of job changes. If participants remove monies from their accounts, they will have lower benefits in retirement.

In summary, available evidence indicates that the proportion of workers who will receive pension benefits in retirement will remain about the same as today unless there are fundamental changes in the national retirement and tax policies. For future retirees who have earned an employer pension, an increasing proportion of them will receive income from defined contribution pension plans, especially 401(k) plans. At present, the impact on pension income of participation in defined contribution rather than defined benefit plans is not known; however, the greater portability of defined contribution plans should enhance the mobility of the work force in the twenty-first century.

Health Insurance for Active Workers

Company-provided health insurance is central to U.S. health care system as most nonelderly Americans receive health insurance through their company or through dependent coverage based on the employment of a family member. Several significant changes are occurring in employer-provided health insurance. First, there has been a sharp decline in the proportion of workers participating in company health insurance plans in the 1990s. Second, company-provided health insurance has rapidly moved from fee-for-service plans to managed care plans. Finally, employers are shifting an increasing proportion of the cost of health insurance to workers.

The proportion of full-time workers in firms with more than 100 employees who are participating in a company health plan declined from 92 percent in 1989 to 76 percent in 1997 and a similar although somewhat smaller decline is observed among workers in smaller firms (See Table 3). This decline reflects fewer firms offering health insurance and fewer workers choosing to participate in plans when offered. One of the key factors reducing participation in firms that offer health insurance is the increased cost borne by the employee. Among firms with 100 or more employees, the proportion of employees who were required to make a direct contribution for coverage rose from 52 percent in 1989 to 69 percent in 1997 and the proportion required to make an employee contribution for dependent coverage also increased. The annual contributions to health care plans by employees also has increased (Scofea, 1994; U.S. BLS, 1990, 1998b). Higher employee cost are associated with reduced participation among those workers employed by companies that offered health insurance.

Table 3
Participation in Company-Provided Health Insurance Plans

Medium and Large Firms	1989	1991	1993	1995	1997
Percent of Full-Time Employees Participating in Plan	92	83	82	77	76
Employee Contribution Required for:					
Worker Coverage	52	59	61	67	69
Dependent Coverage	69	74	76	78	80
Type of Plan:					
Fee-for-Service	74	67	50	37	27
HMO	17	17	23	27	33
PPO	10	16	26	34	40

Small Firms	1990	1992	1994	1996
Percent of Full-Time Employees Participating in Plan	69	71	66	64
Employee Contribution Required for:				
Worker Coverage	41	47	52	52
Dependent Coverage	67	73	75	75
Type of Plan:				
Fee-for-Service	74	68	55	36
HMO	14	14	19	27
PPO	13	18	24	35

Source: Various years of U.S. Bureau of Labor Statistics, *Employee Benefits in Medium and Large Private Establishments*, *Employee Benefits in Small Private Industry Establishments*, and *Employee Benefits in State and Local Governments*.

The 1990s has also seen a dramatic change in the type of health insurance received by most workers. In 1989, 74 percent of full-time employees in firms with 100 or more employees who were covered by health insurance were enrolled in a fee-for-service plan, 17 percent were in HMOs, and 10 percent in PPOs. By 1997, the proportion of health care participants in fee-for-service plans had plummeted to only 27 percent while 33 percent were in HMOs and 40 percent were in PPOs (see Table 3).

Substantial variation in health insurance coverage also exists across social and demographic characteristics. In 1995, 148 million nonelderly Americans had some type of employer-provided health insurance. This represented 64 percent of the population with 33 percent receiving coverage on the basis of their own employment and 31 percent being covered as dependents of a worker with health insurance coverage provided by their employer (EBRI, 1997).¹³

Does coverage by health insurance reduce mobility? Does the lack of health insurance encourage job changes? Workers must consider the total value of working for a company as well as the expected value of alternative employment opportunities. Of course, the value of health insurance is likely to play a role. The effect of health insurance arises because not all firms offer health insurance, there is no national health insurance plan, and purchasing health insurance on the private market can be very expensive. A series of recent research studies have examined the impact of health insurance on job mobility. These studies can be separated into two groups, those that find a large and significant effect that coverage by health insurance on the present job is associated with a lower probability of changing jobs (Madrian, 1994; Cooper and Monheit, 1993; Buchmueller and Valletta, 1996) and those studies that find no evidence to support claims that health insurance is associated with reduced turnover (Holtz-Eakin, 1994; and Kapur, 1998). Efforts to reconcile these conflicting findings have as yet been unsuccessful (Currie and Madrian, 1998).

Retiree Health Insurance

Some firms offer health insurance coverage to both active and retired workers.¹⁴ Employer-provided health insurance is a valuable benefit to workers and can influence job turnover and the timing of retirement.¹⁵ Recent surveys by Foster Higgins & Co. indicated that the average cost per retiree for such coverage in 1996 was \$5,210 for retirees under the age of 65 and \$1,874 for persons 65 and over who were eligible for Medicare (EBRI, 1997).¹⁶ The value to retirees may exceed these company costs because the cost to the individual of purchasing similar private insurance would be much higher. Some companies terminate coverage for retirees at age 65 when they become eligible for Medicare.

Coverage by a company health insurance plan is a significant benefit for older persons and directly affects their economic well-being in retirement. The generosity of retiree health insurance is not linked to previous earnings as workers typically receive the same coverage regardless of their pre-retirement salary. Thus, for persons covered by these plans, retiree health insurance is relatively more important for low wage workers. Generally, workers in firms with retiree health insurance are able to retire and retain coverage only if they have met certain age and service conditions. These eligibility conditions are often the same as those for receipt of a pension benefit. Typically, active workers receive the same health insurance coverage regardless of their earnings, years of service with the firm, or their position in the company. Similarly, all retirees usually receive the same coverage. Thus, there is no reduction in benefits for early retirement, fewer years of service, or lower earnings. There are no federal requirements for vesting in retiree health plans.

The promise of future health insurance may reduce the likelihood that workers will quit prior to the age at which they are eligible to retire and continue their health insurance coverage.¹⁷ After the worker becomes eligible to retire and immediately receive retiree health insurance, the probability of retirement increases.¹⁸ Limited evidence also indicates that employers view retiree health insurance as an important component of their retirement policy and these plans are often offered in conjunction with pension plans (Clark, Ghent, and Headen, 1994).

Fewer than half of full-time workers are covered by retiree health insurance programs and a higher percentage of employees in large firms are provided this benefit. Coverage is also higher for persons with higher annual earnings (U.S. Department of Labor, 1994a). Workers

with longer tenure and unionized workers were also more likely to have retiree health insurance (EBRI, 1997). Thus, the inclusion of the value of retiree health insurance will tend to increase difference in economic well-being among retirees.

Retiree health insurance coverage has been declining since the mid-1980s. Data from the Employee Benefit Survey of Medium and Large Firms show that the proportion of full-time workers covered by retiree health insurance declined by about ten percentage points during the last half of the 1980s (Clark, Ghent, and Headen, 1994). Coverage data, shown in Table 4, indicate that the proportion of active employees who are participating in employer-provided medical insurance plans in which these plans extend coverage to retirees has remained relatively stable in the 1990s; however, the proportion of workers who are covered by medical insurance plans has declined slightly. Thus, the proportion of workers covered by retiree health insurance has declined. Surveys conducted by Foster Higgins & Co. also indicate that the proportion of large employers that provided retiree health insurance policies declined from 46 percent in 1993 to 41 percent in 1995 (EBRI, 1997).

Table 4
Percent of Full-Time Employees in Medium and Large Private Establishments Offered Retiree Health Insurance

Type of Coverage	1989	1991	1993	1995	1997
Percent with medical insurance	92	83	82	77	76
Percent of employees with medical insurance that have retiree health insurance:					
Persons less than 65	40	42	44	46	-
Persons 65 and over	35	40	41	41	-
Percent of full-time employees with retiree health insurance*					
Persons less than 65	37	35	36	35	-
Persons 65 and over	32	33	34	27	-

*The proportion of employees with retiree health insurance is calculated by multiplying the proportion of employees with medical insurance times the percent of those with medical insurance that have retiree health insurance.

Source: Various years of U.S. Bureau of Labor Statistics, *Employee Benefits in Medium and Large Private Establishments*, Washington: USGPO.

In addition to the decline in the proportion of the labor force covered by retiree health insurance plans, companies that have retained their plans have shifted a greater proportion of the cost of medical care to retirees. A large proportion of those plan sponsors that previously paid the entire cost of the health insurance now require workers to pay a portion of the cost of this insurance.¹⁹ As with their coverage for active workers, many companies have also changed their retiree health plans from traditional fee-for-service to some type of managed care plan.

The decline in coverage is attributable to rapid increases in the cost of providing health insurance over the past decade, an increase in the ratio of retirees to active workers, reductions in Medicare, clarification of the legal obligation of employers to continue to provide these plans, and changes in the accounting requirements concerning the liabilities associated with these plans. The increase in cost to employers of providing health insurance has resulted in a decline in the provision of this benefit to active workers and retirees. In addition, companies have been changing their health care plans away from traditional fee-for-service plans by requiring workers to enroll in HMOs or PPOs.

When retiree health plans were first introduced, many sponsoring firms had relatively small ratios of retirees to active workers. Thus, the added cost of retiree health insurance was relatively small. With the aging of the population and the maturing of sponsoring firms, the cost of retiree health insurance compared to health insurance for active workers increased. In response, many firms began to rethink their position on retiree health insurance.

Most retiree health plans are closely linked to Medicare by covering medical payments that are not reimbursed by Medicare. Reductions in Medicare coverage during the past decade have meant that company costs have risen. Higher costs coupled with expectations for further reductions in Medicare coverage may have also encouraged firms to reduce or eliminate their own health insurance coverage.

The adoption of FASB Statement No. 106, “Employers’ Accounting for Postretirement Benefits Other Than Pensions” in 1990 dramatically altered the reporting standards for retiree health insurance. Prior to this time, most firms simply reported current expenses for retiree health insurance. FASB 106 required that firms recognize accrued liabilities associated with their retiree health plans on their balance sheets. This ruling resulted in many firms acknowledging large liabilities for these plans and also changed how these plans were viewed by many corporate leaders.

Each of these factors increased the costs associated with offering retiree health plans. In response, many firms eliminated their retiree health plans or modified them to shift costs from the firm to the retiree. The likelihood of future expansion of retiree health insurance is low. Despite the recent reduction in the rate of increase in medical cost, expectations are that the cost to employers of providing health insurance will continue to exceed the rate of inflation. Further reductions in Medicare are more likely to exacerbate the decline in coverage than to stimulate employers to make up the difference in gaps in health care coverage. To the extent that retiree health insurance reduces mobility, the decline in the proportion of the work force with this benefit should enhance mobility in the twenty-first century.

Prospects for Increased Portability of Benefits

Pensions and health plans are offered by many employers as part of labor compensation. These benefits are included in compensation packages because they help firms attract and maintain quality workers. These plans impose substantial capital losses on workers who change employers and can affect the worker's decision to remain with the company. Government policies can and do restrict company choices concerning plan provisions. Regulations can be used to moderate or eliminate the benefit costs of changing jobs. In this section, potential policy initiatives to enhance the portability of pension and health benefits are examined.

Pension Policies and Regulations

Major policy changes could significantly alter employer decisions to offer pension plans, to offer a particular type of plan, or to offer a more generous and portable pension. These changes would also alter the incentives for workers to participate in pension plans, to delay some of their compensation until retirement, and to remain with the firm until retirement. Policy alternatives for earlier vesting, enhanced portability, and increased coverage are reviewed and evaluated.

Vesting

Prior to the passage of ERISA, there were no required standards for the vesting of pension benefits. Some plans had very long vesting periods and others essentially required participants to remain with the firm until the specified retirement age in order to receive a benefit. ERISA established a 10 year vesting standard which greatly reduced the loss in pension benefits for many workers who changed jobs. The Tax Reform Act of 1986 reduced the maximum allowable vesting standard to five years of service thus insuring that additional departing workers would be eligible for future retirement benefits. With a five year vesting standard, most workers who have accumulated any significant pension accruals will be eligible to receive a deferred benefit at retirement. Currently, many defined contribution plans have full vesting prior to five years, with many allowing for the immediate vesting of benefits. All

employee contributions are immediately 100 percent vested. In contrast, virtually all defined benefit plans impose five year vesting.

Periodically, proposals are made to reduce the vesting period to three years or even one year. To date, these proposals have not received much attention. This is due, in part, to the relatively small impact of a shorter vesting period on the value of pension benefits foregone by workers when changing firms. For example, consider a worker aged 35 with three years of service and annual earnings of \$30,000 per year. Assume that the worker is covered by a defined benefit plan with benefit formula that provides 1.5 percent of final salary per year of service beginning at the normal retirement age of 65. The annual retirement benefit available at age 65 based on service to date is \$1,350. Using an interest rate of 6 percent to calculate the deferred vested benefit yields a present value of vested benefits of approximately \$2,700.²⁰

Under the current vesting standard of five years, this worker would forfeit her claim on these funds if she left her employer. If a three year vesting standard was established, she could change jobs and still expect to receive a benefit from this firm in retirement. The loss in pension benefits in this example represents less than 10 percent of one year's earnings and is not likely to be a major deterrent to a worker from moving to another job that is more desirable or one that is expected to pay higher wages.

This example shows that lowering the maximum vesting standard from five years to three would modestly reduce the cost of changing jobs for workers with less than five years of tenure and increase the expected retirement benefits for mobile workers. With a vesting standard of one year, the pension loss for workers leaving after only one year on the job would be reduced by less than \$1,000. The relatively small size of these effects is one of the primary reasons that proposals for reduced vesting have not been enacted and other aspects of pension regulations continue to receive much more attention than do proposals to lower the vesting period.

Portability and Lump Sum Distributions

The primary loss in pension benefits associated with job changes is the lack of portability of pension credits across defined benefit pension plans. As described earlier in the paper, the loss in life time pension benefits is due to the use of benefit formulas that are based on final average earnings. As a result, workers who remain with a single firm over their career earn one pension benefit based on their earnings just prior to retirement. In contrast, workers who change

jobs several times (even if all firms have identical pension plans) will accumulate several pensions but all but the last pension will be based on earnings many years earlier. Therefore, movers will accumulate lower total pension benefits than stayers due to this lack of portability.

The lack of portability could be addressed with several different policies. First, the indexing of deferred vested benefits could be required as a condition for being a qualified pension plan. This would drastically reduce or eliminate the loss in pension wealth associated with job changes. This type of indexing would mean that deferred vested benefits would increase with inflation or some measure of wage growth. While such a policy change would make defined benefit pensions portable, it would also institute a substantial new cost of offering defined benefit plans that would be paid either by the firm the worker was leaving or by the workers new employer.

If government policy required the old firm to pay for this indexing, the added cost would cause many more employers to terminate their defined benefit plans. These companies might then establish defined contribution plans to replace the terminated defined benefit plans. If new employers had to pay for this indexing of benefits earned on earlier jobs, they would be much less likely to hire such employees. This would further reduce employment opportunities for older workers. Thus, true portability of pension benefits in defined benefit plans could be required through further regulations, however, such a policy would adversely affect pension coverage and exacerbate the trend toward increased use of defined contribution plans.

Another issue related to the value of benefits for departing workers concerns the immediate access to the value of their deferred vested benefit. Upon leaving the company, some worker would prefer to have these funds give to them for immediate use or to be rolled over into a new pension account. McGill, et al. (1998) report that over 40 percent of large sponsors of defined benefit plans provide some lump-sum options and most defined contribution plans allow for the disbursement of plan assets when employment is terminated. Thus, many pension participants who change employers are denied access to their pension funds until retirement.

The lack of access to pension funds is an issue that primarily confronts participants in defined benefit plans. This lack of access may encourage some workers to remain with their current firm rather than seeking new employment. The government could institute a policy requiring that all workers have the option of a lump sum distribution when they leave an employer.

Are lump sum distributions sound retirement policy? Many argue that workers know what is in their best interest and they can decide whether to leave their retirement benefits in the existing plan or whether to withdraw these funds. If the funds are invested and saved for retirement, the worker could accumulate greater retirement savings if the rate of return on the new investments exceeds the interest rate used to calculate the lump sum distribution, obviously, they might also earn lower returns and thus have a lower retirement income. Many retirement specialists fear that individuals will spend these disbursement rather than save them and as a result, retirement income will be lower. In either cases, greater availability of lump sum distributions would tend to reduce the perceived loss in pension wealth with job changes and should increase mobility. Whether a policy promoting lump sum distributions is good retirement policy is debatable.

Coverage

Government policies to increase pension coverage can be sorted into three groups: policies that would required employers to offer a pension, new incentives to encourage employers to offer pensions, and changes in tax and social security policies that would affect the desirability of pensions for workers and firms.

One problem confronting pension participants who are considering changing employers is that many companies do not provide any pension plan. Thus, the move from one employer to another may result in the loss of pension coverage. The only way to completely eliminate this problem is to require all firms to offer some type of pension. The President's Commission on Pension Policy appointed by President Carter in the 1970s recommended such a policy of mandatory pensions.

The Commission proposed that all firms without a pension plan must participate in a universal defined contribution plan based on a minimum 3 percent payroll contribution. All benefits would be immediately vested. Under this plan, workers would have individual accounts that would not be affected by their changing employers – the universal pension would have been fully portable (President's Commission on Pension Policy, 1981). This plan was widely debated and ultimately rejected. Since the failure of the commission's recommendation, no serious consideration has been given to mandating employer pensions. The main arguments against

mandatory pensions are the increase in cost that they impose and the impact on employment in small firms.

If pensions are not mandated, how can pension coverage be expanded? The government could encourage firms to provide pensions through the implementation of new tax incentives or reductions in the regulatory costs associated with pensions. Given the existing preferential tax incentives for pensions, it is unlikely that further incentives will be provided in the tax code. In fact, some analysts (Munnell, 1989) argue that rather than expanding the preferential tax status of pensions, Congress should amend the tax code so that pension contributions and the earnings of pension fund be treated as ordinary income for tax purposes.²¹

Reducing or eliminating the regulatory cost of meeting existing standards would provide a further incentive for companies to offer pensions. In the past, Congress has granted administrative relief to small businesses in an effort to encourage them to provide pensions for their workers through the use of simplified employer pensions (McGill, et al., 1996). Consideration of new policies to eliminate impediments to pension coverage among small employers is on-going. Some analysts worry about the increased prospects for abuse with fewer regulations while others concentrate on the need to expand pension coverage. Without further incentives or simplified regulations, it is doubtful that pension coverage will expand among small employers.

Several changes in national tax policy are now being debated. If enacted these tax reforms would alter the demand for employer pensions. One such policy is to shift from the current income tax to a consumption tax. A consumption tax would tax expenditures rather than income. With a consumption tax, a worker's earnings that were saved privately for retirement would have the same tax status as current employer provided pension plans. In such an environment, employer pensions would be less desirable to workers because they would have the alternative of developing their own retirement plans with pre-tax dollars.

A second less comprehensive proposal is to retain the current income tax structure but make pension contributions and pension fund earnings taxable. Implementation of this policy would also equalize the tax status of private saving and employer-provided pension plans. Either of these changes would reduce the desirability of employer provided pensions relative to private savings. Such a change in tax policy probably would result in fewer retirees having pension benefits in the future; however, the decline in pension benefits might be somewhat offset by

greater private savings. This private response would be greater with the adoption of a compensation tax which would raise the net return to private savings. Eliminating the preferential tax status of pensions within the income tax code would leave the net return to private savings unchanged while raising the cost of saving for retirement through employer pensions.

Changes in Social Security policy also impact the preferences for pensions of both workers and firms. Significant reductions in Social Security benefits might encourage firms and workers to expand employer pensions so that total retirement benefits remain relatively constant and from the firm's perspective, older workers would continue to have appropriate retirement incentives. Employers develop human resource policies in order to achieve various strategic objectives within the context of required programs such as Social Security, Medicare, and Unemployment Insurance. Changes in these programs alter total compensation from working and incentives that may influence worker behavior. Managers may attempt to offset the new incentives associated with the changes in governmental policies. For example, if modifications to the Social Security benefit formula or the normal age of retirement provide incentives for older persons to remain on the job, employers may seek to undo this incentive by altering their pension and retirement policies. The size and significance of this response remains to be seen.

Other Regulatory Changes

Further government regulation of pensions that raise their administrative costs would result in lower coverage in the twenty-first century. Since the passage of ERISA, periodic changes in pension regulations have added to the administrative cost of pension plans making them less desirable to firms (and workers if administrative costs are passed on to employees in the form of lower benefits or lower wages). Policy makers must recognize that pensions are voluntary benefits and that the introduction of new regulations on defined benefit plans, no matter how well intended, may reduce the likelihood that companies will provide these plans in the future.

If future regulations fall most heavily on defined benefit plans, as they have in the past, the movement toward greater utilization of defined contribution plans will be accelerated. Such regulations typically result in greater increases in the administrative costs for smaller firms and would, therefore, likely accelerate the disappearance of defined benefit plans among small

employers. The introduction of and frequent changes in government regulations of pensions contributed to the ending of the expansion of pensions coverage during the last 25 years and the shift toward greater reliance on defined contribution plans.

Summary

This section has reviewed a variety of proposals that might reduce or eliminate the loss of pension benefits associated with job changes. It is important to remember that this is not the sole (or perhaps, even the primary) focus of pension policy. Workers desire employer pensions in order to more efficiently save for retirement. Congress has encouraged the adoption of employer-based pensions as a central part of our national retirement policy. Thus, in considering policies to increase the portability of pension benefits, we should not lose sight of the goal of providing an adequate retirement income.

Policies that enhance portability of benefits for those covered by a pension but result in fewer firms offering pensions are not necessarily good public policies. Similarly policies that further regulate defined benefit plans, such as those that require indexing of deferred vested benefits or immediate vesting, may result in a greater reliance on defined contribution plans. Whether this tradeoff is desirable is also debatable. It is ironic that many of those proposing new regulations are strong proponents of defined benefit plans and prefer these plans to defined contribution plans. In assessing the impact of new pension mandates it is important to remember that pensions are not required by law but are voluntary benefits. In the face of higher administrative costs and reduced flexibility, existing plan providers may simply decide to eliminate their plans, new firms may opt not to establish plans at all, and other firms will continue to shift to the use of defined contribution plans, stock options, and other forms of incentives.

Health Insurance

In the United States, company-provided health insurance is the primary method that nonelderly Americans acquire health insurance. However, not all companies offer health insurance and the quality and value of employer plans is quite different. Workers currently covered by employer-provided health insurance must consider the impact changing employers will have on their access to health insurance. The portability of health insurance has been

addressed by the passage of COBRA and HIPAA. COBRA allows job changes to retain coverage under their former employer's health plan for up to 18 months but with the individual paying the full cost of this insurance. HIPAA reduces the problems associated with moving across health plans associated with pre-existing health conditions.

The main problem currently facing those considering a job change is whether potential new employers will offer health insurance and whether this health insurance will be of the same quality as that in the current job. The only real solution to this problem is the adoption of a national health insurance program where all employers were required to provide a minimum health insurance plan. Proposals by the Clinton administration for this type of national health insurance ended in failure and reconsideration of such plans in the near future seems doubtful.

Endnotes

¹ Wages and salaries represented only 71.9 percent of private industry costs per hour worked for labor compensation in 1996. Expenditures for retirement and savings plans accounted for 3.1 percent and employer costs for health insurance were 5.9 percent of total employer costs. The proportion of total employer costs devoted to these benefits was higher in larger companies (EBRI, 1997).

² The service-producing sector includes transportation, communications, utilities; wholesale trade; retail trade; finance, insurance, and real estate; service; federal government; and state and local government. The goods-producing sector includes mining; construction; and manufacturing.

³ There is considerable debate over the magnitude and composition of any trend toward decreased job tenure and a decline in the presence of long career jobs. Allen, Clark, and Schieber (1999) provide unique analysis of the changes in tenure for 51 large firms that questions whether the labor force is becoming more mobile in this sector of the economy.

⁴ Firms are able to deduct contributions to qualified pension plans as a business expense in the determination of corporate income tax. Neither these contributions nor the earnings on the pension funds are counted as current income for workers. In addition, qualified employee contributions to pension plans are also made with pre-tax dollars. Pension benefits are considered taxable income when they are received. Thus, tax payments are deferred until actual receipt of pension payments.

⁵ McGill, et al., (1996) provides a comprehensive discussion of these two types of pension plans and the federal regulations concerning them. Also see Olsen and VanDerhei (1997) for a discussion of the differences in the two types of plans and the increasing dominance of defined contribution plans.

⁶ Other types of formulas in defined benefit plans include: benefits based on career average earnings and a flat dollar amount per year of service. This latter type of formula is often used in collectively bargained plans. See U.S. Bureau of Labor Statistics (1998b) for a detailed description of the characteristics of defined benefit plans and their incidence among workers employed by medium and large employers.

⁷ Defined contribution plans include money purchase plans, profit sharing plans, employee stock ownership plans, and 401(k) plans.

⁸ Companies may also use a graded vesting scale under which the worker is 20 percent vested after three years and 100 percent vested after seven years of services. Most firms have chosen to adopt the five year-100 percent vesting standard.

⁹ Some departing workers have the option of taking the present value of these future benefits in the form of a lump sum distribution. It is important to recognize that even in this case, mobile workers will have lower lifetime pension wealth than workers who remain with a single employer.

¹⁰ Many pension participants simply take the lump sum distribution and do not roll these funds into a new pension account. These lump sum distributions are subject to current income tax and penalties for early withdrawals.

¹¹ Detailed studies of trends in pension coverage are presented in papers in U.S. Department of Labor (1992, 1994b).

¹² Also see U.S. Department of Labor (1994a) for an analysis of the 1993 CPS concerning coverage rates. U.S. Department of Labor (1993) examines coverage rates using the 5500 tax reporting forms and finds similar relationships to those reported for the CPS.

¹³ An additional 16 million nonelderly Americans purchased health insurance privately. EBRI (1997) also found that 40 million nonelderly or 17 percent of the population did not have any health insurance.

¹⁴ For a general description of retiree health insurance plans, see EBRI (1989) and Warshawsky (1992).

¹⁵ See Currie and Madrian (1998) for an excellent review of the literature on health insurance and labor supply.

¹⁶ The lower cost for older retirees is due to the linkage of employer provided health insurance with Medicare. For retirees (although not for workers), Medicare is the primary payer of medical bills so that the company insurance only pays for the expenditures not covered by Medicare.

¹⁷ As the worker approaches being able to retire and immediately receive retiree health insurance, the incentive to remain on the job increases. Consider the case of a person age 53 with 28 years of service who is covered by a plan that allows a retiree with 30 years of service to begin benefits at age 55; however, if they leave the company before age 55, they must wait until age 62 to receive such coverage. The added value of working two more years includes health insurance coverage for seven years (from age 55 to 62). Also see Currie and Madrian (1998).

¹⁸ Retiree health insurance moderates the decline in economic status after retirement. Most studies find that retiree health insurance coverage significantly increases the probability of retirement (Gruber and Madrian, 1995; Karoly and Rogowski, 1994; Blau and Gilleskie, 1997).

¹⁹ Among workers in medium and large firms with health insurance coverage in 1995, 41 percent were in plans that provided retiree health insurance to persons aged 65 and older. Of those with retiree health insurance only 22 percent were in plans that were fully paid by the employer. In 1989, 47 percent of workers with retiree health insurance were in plans where the employer paid all of the costs (U.S. Bureau of Labor Statistics, 1990, 1998b).

²⁰ This value is based on an annual benefit of \$1,350 ($\$30,000 \times 0.015 \times 3$) payable at age 65 for an expected lifetime of 20 years discounted back to age 35. The loss of pension wealth to this employee would be greater for a more generous pension, an earlier retirement age, higher annual earnings, and a lower interest rate.

²¹ The primary argument is that the tax treatment of pensions results in considerable loss of tax revenues and the advantage of these pension tax expenditures accrue to middle and upper income families. See, Clark and Wolper (1997) for a detailed discussion of the issues associated with pension tax expenditures.

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